Supreme Court, U. S.
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No. 79-2027

In the Supreme Court of the United States

OCTOBER TERM, 1979

FRANCES M. ANDERSON, INDIVIDUALLY AND AS LEGAL REPRESENTATIVE OF THE ESTATE OF PAUL H. ANDERSON, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

HERBERT E. AND MARY C. WIESE, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

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The petition in these federal income tax cases presents the narrow factual question whether amounts received by petitioners[1] upon the sale of their interest in the stock of

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[1] "Petitioners" include Paul H. Anderson, one of the original parties, who died during the pendency of this litigation. His estate has been substituted as a party.

H. E. Wiese, Inc., were "from sales or other dispositions pursuant to binding contracts * * * entered into on or before October 9, 1969" (Section 1201(d)(1) of the Internal Revenue Code of 1954 (26 U.S.C. (1970 ed.)), so as to be subject to taxation at the old capital gains rate of 25%, rather than the new rate of 32½%, on capital gains in excess of $50,000. 26 U.S.C. (1970 ed.) 1201(c)(2)(B).[2]

The pertinent facts are as follows: Petitioners were the principal shareholders of H. E. Wiese, Inc. On March 27, 1969, they agreed to sell their stock in H. E. Wiese, Inc., to another corporation, the Pace Company Consultants and Engineers. The agreement was embodied in two related documents, a "Stock Purchase Agreement" and a "Pledge and Trust Agreement." These documents provided that the sale was contingent upon Pace's sale of its own stock to acquire the funds needed for the purchase of the H. E. Wiese, Inc. shares (Pet. Supp. App. 4-6)[3].

Pursuant to these agreements, petitioners' stock was transferred to a bank serving as a trustee, and petitioners Herbert E. Wiese and Paul H. Anderson, the principal

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[2]Subsequent amendments to the Internal Revenue Code indicate that the question presented has no continuing administrative importance. The relevant provisions of Section 1201(d) were repealed by Section 1901(a)(135)(C)(i) of the Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1787. Thereafter, Section 401(a)(1) of the Revenue Act of 1978, Pub. L. No. 95-600, 92 Stat. 2866, repealed the noncorporate alternative tax for capital gains entirely, effective for taxable years after December 31, 1978. Section 401(c), Revenue Act of 1978, Pub. L. No. 95-600, 92 Stat. 2867.

[3]"Pet. Supp. App." refers to petitioners' unpaginated supplemental appendix, as to which we have supplied page numbers. That supplemental appendix sets forth the Tax Court's memorandum findings of fact and opinion in this case filed on November 29, 1976. By Memorandum Sur Order and Order of February 3, 1977, the Tax Court amended in part its findings of fact. We have set forth this amendment to the Tax Court's findings of fact at App., *infra*.

officers and shareholders of H.E. Wiese, Inc., resigned from its board and took reductions in salary and bonuses to approximately half their former levels. Moreover, both H. E. Wiese, Inc., and Pace incurred substantial costs in undertaking the projected integration of the companies (Pet. Supp. App. 6-7; App., *infra*, 3a, 4a-5a).

By October 1969, however, it became obvious that Pace could not successfully fulfill the contractual condition of making a public offering of its stock, and, during that month, the parties to the proposed sale began to explore alternative methods of effecting the sale (Pet. Supp. App. 10-16). On November 6, 1969, petitioners and Pace signed an agreement which expressly "terminated and cancelled" both of the March 27 agreements (Pet. Supp. App. 16). Thereafter, petitioners Herbert E. Wiese and Paul H. Anderson were restored to the board of H. E. Wiese, Inc., and their stock was returned to them by the trustee. Six days later, on November 12, 1969, the parties signed new agreements which gave Pace an option to buy the H. E. Wiese, Inc. stock until October 15, 1971 (Pet. Supp. App. 17-18). Finally, on October 18, 1971, a sales agreement was executed and the transfer of stock occurred the same day (Pet. Supp. App. 18, 23-24).

Petitioners reported the income taxes resulting from the gain upon the sale of their stock at a rate of 25%, which was available only for gains from sales of capital assets "pursuant to binding contracts * * * entered into on or before October 9, 1969 * * *." 26 U.S.C. (1970 ed.) 1201(d). On audit, the Commissioner of Internal Revenue determined that the gain from the sale of the stock resulted from a sale pursuant to an agreement entered into after October 9, 1969, so that the 25% capital gains rate was not available (Pet. Supp. App. 24). In this suit brought by petitioners for redetermination of the resulting

deficiencies, the Tax Court upheld the Commissioner's determination and the court of appeals affirmed *per curiam* (Pet. App. ii).

1. The decision below correctly rejected petitioners' claim that the November 6 agreement, which expressly "terminated and cancelled" both of the March 27, 1969 agreements, in fact did "nothing more than relieve the Trustee of his fiduciary obligations under the March 27, 1969 * * * Agreement" (Pet. 33-34). The Tax Court's ruling was a finding of fact as to petitioners' intentions, which is subject to reversal only if shown to be clearly erroneous. *Bay Sound Transportation Co.* v. *United States*, 410 F. 2d 505 (5th Cir.), cert. denied, 396 U.S. 928 (1969); see *Commissioner* v. *Duberstein*, 363 U.S. 278, 291 (1960). Here, the Tax Court took note of the express language of the November 6 agreement, as well as of later statements by petitioner Wiese. It found that while the parties had undertaken substantial effort and expense and continued to plan for consummation of the sale, they expressly disavowed the March 27 agreements as a means of doing so.[4] Moreover, the facts that petitioners Herbert

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[4]Accordingly, petitioners err in suggesting (Pet. 38-42) that they were bound on promissory estoppel grounds to negotiate a final sale. By their terms, enforceability of the March 27 agreements was contingent upon Pace's offering of its stock, a condition which did not come to fruition. Petitioners further urge (Pet. 42-43) that the form of the November 6 termination agreement be ignored in favor of what they claim to be the "substance" of the transaction. But in so contending, petitioners ignore the fundamental proposition that they are not entitled to disregard the form in which they have cast a transaction in order to achieve a different tax result. *Commissioner* v. *Nat. Alfalfa Dehydrating*, 417 U.S. 134, 149 (1974); *Gray* v. *Powell*, 314 U.S. 402, 414 (1941); and *Federal Bulk Carriers, Inc.* v. *Commissioner*, 558 F. 2d 128, 130 (2d Cir. 1977) ("these knowledgeable parties cast their transaction voluntarily into a certain formal structure * * *. Having done so, they should be and are, bound by the tax consequences of the particular type of transaction which they created").

E. Wiese and Paul H. Anderson returned to their former positions and salary levels with H.E. Wiese, Inc. and that the trustee returned the stock to petitioners, provide an ample basis to support the Tax Court's finding as to the effect of the November 6 agreement. While the March 27 agreements may have been "binding contracts," entered into on or before October 9, 1969, the 1971 sale of the stock was not made pursuant to these agreements, because these agreements were specifically abrogated on November 6, 1969.[5] Accordingly, petitioners' transaction was not eligible for the lower capital gains rates pursuant to Section 1201(d).[6]

2. The decision below also correctly rejected petitioners' argument (Pet. 43-49) that the Commissioner should be estopped from claiming that the March 27 agreements were terminated by the November 6, 1969 agreement because an Internal Revenue Service agent in 1970 had claimed that the sale was not so terminated but rather "has not been abandoned" (Pet. Supp. App. 20). The agent had done so in urging that H.E. Wiese, Inc., should have capitalized certain legal and accounting fees

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[5]To the extent that petitioners' arguments imply that there were other agreements, effective August 12, 1969, or October 8, 1969 (Pet. 20, 34), they are without merit. The agreement entered into on August 12, 1969, merely extended the dates prescribed by the March 27 agreements, which, as noted above, were later terminated (Pet. Supp. App. 10-11). Moreover, the Tax Court found that an alleged binding oral agreement of October 8, 1969 did not exist in light of its finding that the parties intended to be bound not by any oral agreements but rather only by formal signed writings (Pet. Supp. App. 31, 35).

[6]Petitioners' plea (Pet. 31-33) for a liberal construction of the statute ignores this Court's oft-stated rule that "courts are not free to reject that meaning where * * * it appears to be consonant with the purposes of the Act as declared by Congress and plainly disclosed by its structure." *Helvering* v. *Hammel*, 311 U.S. 504, 511 (1941).

(*ibid.*). But petitioners were not parties to that dispute. Hence, they cannot raise estoppel as a bar in this case. See *Garrison* v. *Commissioner*, 52 T.C. 281, 284 (1969) and cases cited therein.[7] At all events, as the Tax Court noted (Pet. Supp. App. 20-22, 44-46, n.7), the Commissioner's disallowance of the deductions claimed by H.E. Wiese, Inc. may well have been based on other reasons having nothing to do with the asserted ongoing nature of the project, *viz.*, that the expenses were incurred for the personal benefit of the shareholders.

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

WADE H. MCCREE, JR.
Solicitor General

AUGUST 1980

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[7]Petitioners misapprehend (Pet. 48-49) the nature and effect of the settlement between the Internal Revenue Service and H. E. Wiese, Inc. The Tax Court record (Ex. 36-AJ) reveals that the settlement was executed as a Form 870 waiver agreement, in which it is stated that the settlement was not a final and binding closing agreement provided for by Section 7121 of the Code (26 U.S.C.) and that neither party would be prevented from further litigating the tax liabilities for that year.

DOJ-1980-08

APPENDIX

UNITED STATES TAX COURT

WASHINGTON, D.C. 20217

Docket Nos. 7317-74
7406-74

HERBERT E. WIESE AND MARY C. WIESE,
ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT

MEMORANDUM SUR ORDER
AND
ORDER

On November 29, 1976, this Court issued its Memorandum Findings of Fact and Opinion in these cases (T.C. Memo. 1976-362), stating that decisions would be entered under Rule 155. Thereafter, but prior to receiving decisions proposed by the parties based upon agreed computations, petitioners filed two motions: a "Motion For Reconsideration Of Findings Of Fact" and a "Motion To Vacate Or Revise Decision". Since no decisions had yet been entered, the Court has treated the second motion as a "Motion For Reconsideration Of The Opinion".[1] In

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[1]It would seem that the proposed decisions subsequently filed merely represented an agreement of the parties in respect of the computations necessary to give effect to the original Memorandum Findings of Fact and Opinion, and were presented to the Court under Rule 155 so that they could be signed in the event that the Court's disposition of the motions would not call for a different result.

response to an order of the Court, the Commissioner has filed replies to both motions.

The Motion For Reconsideration of Findings Of Fact in essence asks the Court to expand its findings to include 17 separately numbered requested additional findings of fact. All but perhaps one of these now requested findings are contained—either verbatim or in substance—in the findings of fact requested in petitioners' original or reply briefs. These requested findings were carefully evaluated during our original consideration of this case.

To the extent that the proposed additional findings are supported by the evidence before us and may not perhaps be otherwise fully reflected in the findings already made, we shall enlarge or modify our findings accordingly. We have concluded to make such additional findings requested by petitioners as are in our judgment warranted by the evidence, notwithstanding that such findings consist in large part merely of raw evidence which we had already taken into account in reaching our conclusion in the Memorandum Findings of Fact and Opinion previously filed herein.

However, many of the additional findings which petitioners request us to make are in conflict with our view of the record. Because we remain satisfied that our original evaluation of the record was, in all relevant respects, a correct one, we reject those proposed additional findings. Moreover, after taking all of the findings and evidence into account, we adhere to our original judgment that the only legally binding obligations—inforce on or before October 9, 1969,—which committed petitioners to sell their stock to Pace were the written agreements of March 27, 1969. Contrary to petitioners' contentions, we did not find any oral agreements, options, or any other arrangements legally

binding upon petitioners (other than the March 27, 1969, written agreements) that were in existence on October 9, 1969,—notwithstanding that there had been discussions contemplating that some type of option agreement would be entered into at a future date. And, the record plainly and convincingly establishes that the March 27, 1969, agreements—the only outstanding legally binding arrangements—were "terminated and cancelled" on November 6, 1969. While petitioners ultimately sold their stock to Pace in 1971, this sale was consummated pursuant to *different* obligations entered into sometime after November 6, 1969. Moreover, because these new obligations were not entered into until after the March 27, 1969, agreements had ceased to have any legally binding effect, petitioners may not prevail in reliance upon any theory that the new agreements were merely "modifications" of the old, within the meaning of section 1.1201-1(f)(2)(ii), Income Tax Regs. In sum, the sale of petitioners' stock was not made under an arrangement by which petitioners were "at all times on and after October 9, 1969, legally bound * * *", as required by the regulations and the statute. The premises considered, it is

ORDERED:

(1) That the following be inserted as the third sentence of the first full paragraph on page 6:

> Both companies incurred substantial costs to develop this information required by the SEC.

(2) That the two complete paragraphs on page 7 be deleted and that the following be included in place thereof:

> In connection with the March 27, 1969, agreements, Mr. Wiese and Mr. Anderson entered into employment agreements which would have had

the effect of reducing substantially the salary and bonus compensation that each of them had enjoyed prior to that date. For the fiscal year ended February 28, 1969, Mr. Wiese received remuneration of approximately $182,458, and Mr. Anderson received remuneration of approximately $130,717. Subsequent to March 27, 1969, the salary to be paid to each man, pursuant to his new employment contract was as follows: Mr. Wiese was to be paid a salary of $31,200 per annum, for a term ending September 30, 1971; and Mr. Anderson was to be paid a salary of $26,000 per annum, for a term ending February 28, 1974. Each man was also to participate in bonuses payable under a new incentive compensation policy which was to be adopted with respect to Wiese, Inc. On the basis of the salaries provided under the employment contracts for Messrs. Wiese and Anderson, and further on the basis of the estimated earnings of Wiese, Inc., for the fiscal year ended February 28, 1969, it was estimated that the total compensation (salary plus bonus under the proposed new incentive compensation policies) which each man would have received for that year would have been as follows: Mr. Wiese, $75,000; and Mr. Anderson, $70,000.

As a result of these changes, the compensation of these two men would have been more nearly commensurate with that received by other Pace executives. The reduction also was supposed to reflect their lessened work-load and decreased responsibilities. However, the record does not disclose the amount of compensation which each man actually received for 1969. See *infra*, p. 16.

As part of the integration of the business activities of Wiese, Inc., and Pace, an engineering design group was established within the Wiese, Inc. organization.

This group was created by the transfer, in July 1969, of Pace's existing Process Design Group to Wiese, Inc. The transferred group consisted of a director of engineering and six project managers and engineers. These seven persons became employees of Wiese, Inc. and their salaries for the period beginning July 1, 1969, and ending December 31, 1971, were paid by Wiese, Inc., in the amounts shown in the following table:

	1969	*1970*	*1971*
R. E. Rimkus	$10,710.00	$34,001.58	$29,061.09
J. A. Askins	9,492.00	17,986.00	20,876.00
L. E. Reisner	6,704.13	14,346.00	15,249.20
R. D. Ostermiller	8,140.00	5,640.00	-0-*
K. D. Brenton	10,168.00	6,768.00	-0-*
D. P. Moore	7,940.00	5,880.00	-0-*
E. H. Carpenter	10,644.00	21,680.00	25,534.54
TOTAL	$63,798.13	$106,301.58	$90,720.83

* Terminated for cause by Pace.

Any profits resulting from the work of the engineering group belonged to Wiese, Inc. However, although it was in all these respects integrated into Wiese, Inc., the group remained under the supervision of Mr. Broyles, who was at all times a Pace employee.

After the initial transfer of these seven employees, Pace supervised the hiring of an additional 40 persons for the engineering group of Wiese, Inc. These 40 people included drafts-men as well as civil, structural, instrument, mechanical, chemical and electrical engineers. It cost approximately $5,000 in addition to regular salary and benefits to hire each engineer. This cost was borne by Wiese, Inc.

The establishment of this engineering division necessitated the expansion of Wiese, Inc.'s administrative office and parking facilities and the relocation of the corporation's equipment, tool and repair shops. In making these adjustments, on the basis of Pace's recommendations, Wiese, Inc., incurred costs of between a quarter and a half million dollars.

The transfer of the seven engineers from Pace to Wiese, Inc., had the effect of reducing Pace's net income by approximately $30,000 annually.

(3) That petitioners' motions are in all other respects denied.

/s/ Arnold Raum

ARNOLD RAUM
JUDGE

Dated: Washington, D.C.
February 3, 1977